

1st Encounter

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FIRST ENCOUNTER OF THE FINANCE MINISTERS OF THE AMERICAS AND THE CARIBBEAN

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Strategic Vision on a Hemispheric Agenda of Cooperation

Discussion Note

Recently, the Latin American and Caribbean (LAC) region has enjoyed strong growth, which has lifted incomes, created employment, and reduced poverty. It has harvested the benefits of stronger macroeconomic positions and improved credibility of policy frameworks. Some countries have also been buoyed by the boom in commodity prices, and rising foreign direct investment (FDI). However, since last year the global expansion is losing momentum in the face of recent financial disturbances, therefore there is a need to develop a new strategic agenda within the region in order to strengthen its position as community of countries.

For instance, strong demand combined with exogenous external shocks, especially to food and fuel prices, has put upward pressure on inflation. This has posed risks for the sustained decline in inflation to the single-digit range, one of the region's most important macroeconomic accomplishments in the past decade. Moreover, high food prices have also had a disproportionate impact on the poor, and governments are required to mitigate these effects.

The shock to housing markets and financial sectors in industrialized countries has thus far had less impact on LAC financial markets and external funding than in past episodes of global financial stress. Domestic money and bond markets remain generally stable. However, external funding conditions have tightened, especially for the LAC corporate sector, though less as compared with other emerging markets. Nevertheless, increasingly cautious investors will be more demanding with conditions offered to all emerging markets, and more volatility is expected in the following years. Thus, we need to strengthen a strategy to maintain our image as a solid and attractive region to invest, while balancing the expected growth slowdown against ongoing inflation pressures and a continuous effort to reduce poverty.

Reaching these goals will require careful policy management within a framework of regional cooperation and coordination:

- Monetary policy. Lately, monetary policy has been oriented toward containing continued pressures on inflation and expectations. Flexible exchange rates would be the first shock absorber in the event of a weaker external environment than envisaged in the baseline.
- Fiscal policy. Compared with the past, there is less need for countries to reduce spending in the face of a cyclical slowdown in revenues, and many have room to allow automatic stabilizers to operate. We have to be cautious against discretionary fiscal stimulus in many countries. Increases in public spending could undermine policy credibility and ultimately have a negative impact on growth as risk premia rise and investment falls in the whole region.

- Financial sector policies. Supervisory authorities are continuing their close monitoring of risks, as well as maintaining a close dialogue with regulators in other countries, given the international nature of the current shocks. Apart from these measures, even closer communication between the region's financial supervisors should be fostered. There is also the need to strengthen competition and increase penetration. Moreover, the financial sector's importance as an instrument to improve people's living standards demands a rapid and sound expansion of financial services.
- Social policies. Addressing the impact of higher food prices on the poor is an important policy concern. Well-targeted cash transfers present an effective policy tool in this regard. However, administrative measures to reduce the pass-through of high food prices risk creating fiscal and quasi-fiscal costs and distorting economic incentives and efficiency.
- Macro externalities. A negative shock in a single country of the LAC sub-region affects the stability of FDI and attractiveness of other countries within the region.
- Infrastructure to compete. LAC's comparative lag of development in this sector demands increasing resources. Sound fiscal policies and the responsible channeling of extra-fiscal resources are needed, complemented with FDI given the sector's high potential, especially in telecomm and energy. Supervisory and regulatory issues need to be addressed.
- Economic integration. Further economic integration is desirable in order to create a regional market for goods and services and take advantage of economies of scale in attending the needs of a large and diverse market. Of particular concern is the fact that protectionistic pressures seem to be increasing in several countries in the region, and an important and concerted effort is required to convince local polities of the benefits of free trade.
- Energy supply. Even though the Western Hemisphere has both large consumers and producers of energy, markets across the region remain highly fragmented and production has recently stagnated in several producing countries. Discussions to promote further integration and development of inter-country markets could lead to large gains in efficiency and certainty of supply, being of particular importance in an environment of increasing energy costs. Collaborative efforts to develop bio-fuels could also lead to significant efficiency gains.
- Regional politics. The region should strengthen the institutions, such as the OAS, that guarantee a peaceful resolution of regional crisis and foster regional cooperation.
- Production and Financing of Regional Public Goods (Health). A common policy for tackling public health issues is deemed necessary in order to avoid the devastating effects of different health crisis. Positive externalities exist in regional vaccination strategies, early warning systems and effective communication of regional public health risks such as existing diseases including dengue fever and malaria, and also potential threats such as avian flu.

- Immigration. A policy to address the issues of immigration is necessary in times of greater flows of individuals between countries due to economic integration and aspirational goals. The respect of basic human rights has to be guaranteed for all immigrants and the legal framework should be strengthened to allow cooperation between countries in order to resolve existing issues.

Issues for discussion

- What are the best mechanisms to design a hemispheric agenda and empower it in international fora and institutions?
- How can the most developed countries of the hemisphere support the implementation of this agenda?
- Would it be convenient to establish annual meetings supported by documents prepared by thematic working groups and specific IFIs research?
- What are the perceived main obstacles for the implementation of infrastructure projects?
- What mechanisms can be established to transmit best practices in the design and implementation of these kinds of projects?
- What “bottlenecks” have been identified in financing infrastructure projects?
- How can IFIs contribute in the design, finance and implementation of the infrastructure projects?
- It is said that competition to attract FDI promotes harmful fiscal practices and the financial regulatory standards weakness. What kind of cooperation can be established to keep an attractive environment for FDI while avoiding these undesirable practices?
- Would it be convenient to adopt principles for a fiscal policy framework to strengthen the positive perception of the hemisphere’s economies in the global economy?
- Is there a need to establish a Hemisphere’s Council of financial regulators to monitor regional developments? Is it feasible?
- Are we converging towards a hemisphere market or towards several sub-regional markets within the region?
- How can we preempt the increasing protectionistic pressures that have arisen in the current context of decelerating global growth and increasing commodity prices? What is the best way of convincing local polities of the large gains that have come due to increasing integration? What are the best ways to compensate those sectors of the economy that have not benefited from freer trade?
- How can we develop more integrated energy markets? Would common efforts to develop bio-fuels lead to more efficient outcomes?

